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88-1604

No.

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1988

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JUDITH DIANE DUFF LEACH, *et al.*,
*Petitioners,*

v.

FEDERAL DEPOSIT INSURANCE CORPORATION, *et al.*,
*Respondents.*

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## PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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## QUESTIONS PRESENTED

1. Whether the rights of shareholders in a banking association created solely by federal authority under the National Bank Act, 12 U.S.C. § 21 *et seq.* to assert causes of action for breach of fiduciary duty, misrepresentation and fraud under RICO, 18 U.S.C. § 1964(c), *et seq.* are determined by state law?

2. Whether a minority shareholder in a federally created banking association has standing to sue for violations of the National Bank Act, when the only injury alleged consists of diminished stock values?

## LIST OF PARTIES

The parties to the proceedings below were the Petitioners, Judith Diane Duff Leach, individually and as next friend of her minor child, Jeremiah Christopher Duff Leach, and as the personal representative of the estate of Arthur James Duff, and Ted E. Duff and the Respondents, Federal Deposit Insurance Corporation, Receiver of Seminole State National Bank, Seminole, Texas; B.C. Clark, Paul Condit, Walker Dearing, Jr., Dwayne Herman, D.G. Hoffman, C.D. Wickson, Jr., Carroll Haralson, Alton Freeman, Reeves Cothes, Sam Spikes, George Shivers, Dr. Joe Cauley, MBank Dallas, Richard Watts, S.H. Hart, Sr., Kenneth Newcomb, R.D. Skelton, Sr., and First West Financial Ventures.

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## OPINIONS BELOW

The opinion of the Court of Appeals for the Fifth Circuit is reported at 860 F.2d 1266, and is reprinted in the appendix hereto, p. Ap.-1, *infra*.

The memorandum decision of the United States District Court for the Western District of Texas (Woodward, D.J.) has not been reported. It is reprinted in the appendix hereto, p. Ap.-17, *infra*.

## JURISDICTION

The judgment of the Court of Appeals was entered on December 2, 1988. A petition for rehearing was filed on or about December 15, 1988, and an order denying same was entered on January 3, 1989.

The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1), p. Ap.-53-54, *infra*. Petitioner further asserts that this Court should grant certiorari to review the Court of Appeals' decision in that it seems to be in conflict with the direction taken or decisions made on this issue in other Courts of Appeals. Further, the decision of the Court of Appeals in this case presents for review a federal question not previously decided by this Court, and is of such importance that this Court should settle this question, S.Ct.R. 17.1 (a)(c), p. Ap.-53, *infra*.

## STATUTES INVOLVED

18 U.S.C. § 1964(c) provides in pertinent part:

> Any person injured in his business or property by reason of violation of § 1962 of this chapter (18 U.S.C. §l 1962) may sue therefor in any appropriate United States District Court and shall recover threefold the damages he sustains in the cost of this suit including a reasonable attorney's fee, p. Ap.-47-48, *infra*.

12 U.S.C. § 93(a) provides in pertinent part:

> If the Directors of any national banking association knowingly violate, or knowingly permit any of the officers . . . to violate any of the provisions of this chapter . . . every director who participated in or assented to the same shall be held liable in his personal and individual capacity for all damages which the association, its sharehodlers, or any other person shall have sustained in consequence of such violation, p. Ap.-48-49, *infra*.

## STATEMENT OF THE CASE

The Petitioners, Judith Diane Duff Leach, individually and as next friend of her minor child, Jeremiah Christopher Duff Leach, and as the personal representative of the estate of Arthur James Duff, and Ted E. Duff, ("Leach") are minority shareholders in the Seminole State National Bank ("Bank"). Leach initiated an action against the former officers and directors of the Bank and MBank Dallas, Texas in the United States District Court for the Northern District of Texas, Lubbock Division. Federal jurisdiction was predicated on alleged violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. § 1961, *et seq.*, p. Ap.-45-47, *infra.*, and federal question jurisdiction, 28 U.S.C. § 1331, p. Ap.-54, *infra.*, based upon allegations of violations of The National Bank Act, 12 U.S.C. § 93 *et seq.*, p. Ap.-48-49, *infra*. The RICO allegations included misrepresentations and breaches of fiduciary duties owed to Petitioners as minority shareholders. The National Bank Act violations alleged include violations of the Call Report Statute, 12 U.S.C. § 161, p. Ap.-54-56, *infra*. A true and correct copy of Petitioner's First Amended Complaint is included in the appendix at Ap.-24, *infra*.

The Federal Deposit Insurance Corporation ("FDIC"), which had been appointed Receiver of the Bank, moved to dismiss under Fed. R. Civ. P. 12(b) (6) p. Ap,-51, *infra*, as did other Defendants, including MBank Dallas. Those defendants contended that Leach lacked standing to pursue either RICO or National Bank Act claims because the claims alleged were derivative and belonged to the Bank, now FDIC as Receiver, not to

minority shareholders in their individual capacities. Because Leach could only show damages in the form of diminished value of her stock, the FDIC argued this type of damage was wholly indicative of injury to the Bank, and not the violation of any fiduciary duty owed to minority stockholders of a national bank. The District Court granted the FDIC and other Defendants' Motion to Dismiss. Thereafter, Leach appealed.

A panel of the Court of Appeals for the Fifth Circuit affirmed the judgment of the District Court, holding that state law determines whether the shareholders of national banks, created by federal law, have been injured in their property by reason of RICO violations. The Court recognized that its holding on this issue implicated a serious problem of uniformity of federal law throughout the states. Nonetheless, the Court concluded, by balancing, that application of state law to determine whether a national bank shareholder has been injured under RICO was preferable to generating federal common law in the area.

Further, the Court also concluded that despite the literal wording of 12 U.S.C. § 93 (a) p. Ap.-48-49, *infra*, which appears to grant standing to national bank shareholders, Leach could not maintain her action for violations of the National Bank Act. The Court reasoned that because all she could show were damages in the form of minished stock value, these damages reflected corporate injury, and thus denied Leach standing. The Court denied arguments that prior precedent in the Fifth Circuit and the Ninth Circuit granted minority shareholders in Leach's position standing to sue under 12 U.S.C. § 93 (a). Instead, the Court adopted the Sixth Circuit position that diminished value to stock was mere corporate injury, and not direct personal injury.

## REASONS FOR GRANTING THE WRIT

### 1. The Decisions of the Court of Appeals as to the Law Governing Standing in a RICO Claim are Apparently in Conflict.

The controlling question here is should the law of particular state govern the rights of shareholders in an association created solely by federal authority, under the National Bank Act, 12 U.S.C. § 21 *et seq.*, p. Ap.-50, *infra?* The general rule is that when a federal statute creates a cause of action or establishes rights under nationwide programs where uniformity is required then federal law — interpreting federal policies — and not state law, controls. *Reconstruction Finance Corp. v. Beaver County, PA*, 328 U.S. 204 (1946); *Burks v. Lasker*, 441 U.S. 471 (1979); *J.I. Case Co. v. Borak*, 377 U.S. 426 (1964); *United States v. Kimbell Foods, Inc.*, 440 U.S. 715 (1979).

The Seventh Circuit in *Schacht v. Brown*, 711 F.2d 1343, 1347 (7th Cir. 1983), *cert. denied*, 464 U.S. 1002 (1983) has indicated that when there is a claim under RICO, the analysis of standing should be governed by federal policy considerations in enforcing federal laws. *See also, O'Donnell v. Kusper*, 602 F. Supp. 619 (N.D. Ill. 1985). The Courts of Appeals for the Fifth, Sixth and Second Circuits have held that the laws of a particular state determine whether a plaintiff has been injured for purposes of standing under RICO. *Gaff v. FDIC*, 814 F.2d 311 (6th Cir. 1987); *Warren v. Manufacturers National Bank of Detroit*, 759 F.2d 542 (6th Cir. 1985); *Rand v. Anaconda-Ericsson, Inc.*, 794 F.2d 843 (2nd Cir. 1986); and *Crocker v. FDIC*, 826 F.2d 347 (5th Cir. 1987).

It is important that standing under 18 U.S.C. § 1964(c) p. Ap.-47, *infra*, be uniform throughout the United States. Relying on the various states' laws to determine the nature and extent of an "injury in business or property" would lead to a lack of uniformity. This is especially true where the rights created for a national bank shareholder arise, as here, solely under federal law, the National Bank Act.

The general rule in most jurisdictions in the United States is that "a shareholder of a corporation has no personal or individual right of action against third persons for damages that result indirectly to the stockholder because of an injury to the corporation." *Twohy v. First National Bank of Chicago*, 758 F.2d 1185, 1194 (7th Cir. 1985). Many jurisdictions subscribe to this general rule. *See Cowin v. Bresler*, 741 F.2d 410, 414 n.6 (D.C. Dir. 1984) citing jurisdictions that subscribe to the general rule. There are exceptions. *Schaffer v. Universal Rundle Corp.*, 397 F.2d 893 (5th Cir. 1968); *Johnson v. American General Insurance Co.*, 296 F. Supp. 802 (D.D.C. 1969); *Yanow v. Teal Industries, Inc.*, 422 A. 2d 311 (Conn. 1979).

When the duty is a fiduciary one, such as here and in *Johnson v. American General Insurance Co., supra*, there is a greater likelihood of confusion. Some states have adopted a statutory definition of the duty owed by officers and directors to corporations. Others have not. In those states which have adopted a statutory scheme, the duties for officers and directors is often very different. Compare Va. Code Ann. § 13.1-690 (Supp. 1985) with Miss. Code Ann. § 79-4-8-30 (Supp. 1987).

Due to this confusion and lack of uniformity in the law to be applied in a RICO standing question, and because the rights of shareholders of federally-chartered banking associations are at issue, the law with respect to this issue should be federal common law. Federal law precedent provides a cause of action for the violation of fidicuiary duties owed to minority shareholders

by officers and directors. *Pepper v. Litton*, 308 U.S. 295, 60 S.Ct. 238 (1939); *Johnson v. American General Insurance Co., supra; First Hawaiian Bank v. Alexander*, 558 F. Supp. 1128 (D.C. Hawaii 1983). In *First Hawaiian*, the court found, using exclusively federal law, a federal interest in the uniform regulation of savings and loan institutions. The interest in uniformity supported recognition of a federal common law cause of action for breach of fiduciary duty. *Id.* at 558. Relying upon *Harmsen v. Smith*, 542 F.2d 496 (9th Cir. 1976), the *First Hawaiian* court allowed a shareholder a direct action even though the damages claimed were diminution in the value of the stockholder's shares. *Id.*

## II. The Limitations Some Circuits Have Placed on RICO Claims Thwart the Congressional Purpose in That They Fail to "Liberally Construe the Act 'to Effect Its Remedial Purposes'".

The so-called "prudential" limitation on standing that was apparently the basis of the panel decision of the Court of Appeals for the Fifth Circuit was developed to prevent multiplicity of actions by numerous shareholders and thereby protect corporate creditors. *See generally*, 12 (B) W. Fletcher, *Cyclopedia of the Law of Private Corporations*, §§5907-5914 (rev. perm. ed. 1984). Although courts are bound by constitutional standing limitations, *Gladstone Realtors v. Village of Bellwood*, 441 U.S. 91 (1979); *Trafficante v. Metropolitan Life Insurance Co.*, 409 U.S. 205 (1972), they are not absolutely bound by "prudential limitations."

A philosophical difference has developed in the circuits. Some have engrafted unintended standing restrictions upon persons who file suit under RICO even though Congress intended RICO to be a remedial statute under which standing issues should be resolved in favor of the wronged as opposed to the wrongdoers. *Compare Haroco v. American National Bank & Trust Company of Chicago*, 747 F.2d 384 (7th Cir. 1984), *aff'd*, 473 U.S. 606 (1985) with *Armco Industrial Credit Corp. v. SLT Warehouse Co.*, 782 F.2d 475 (5th Cir. 1986) and *Rand v. Anaconda-Ericsson, Inc.*, 794 F.2d 843 (2nd Cir. 1983).

Just as this Court resolved the conflict in various federal circuit decisions regarding the question of which limitations period would apply in a RICO action, *Agency Holding Corporation v. Malley-Duff & Associates, Inc.*, 107 S.Ct. 2759 (1987) (Supreme Court adopts Clayton Act four-year limitation period for RICO actions), this Court should also resolve the question of the law to be applied in this case where the sole reason for application of state law by the Fifth Circuit is simply the locale of the Bank in a particular state.

Leach, as a minority shareholder did not benefit from having rights under state law, as none could be conferred. The simple truth is that a shareholder of a national bank gathers no rights from state law. State law did not give the Bank life, nor does there appear any valid reason for state law to be adopted as a surrogate benchmark. The National Bank Act, 12 U.S.C. § 21 *et. seq.* p. Ap.-50, *infra*, constitutes, by itself, a complete system for the establishment and government of national banks. *Deitrick v. Greaney*, 309 U.S. 190, *rehearing denied*, 309 U.S. 697 (1940). A simple review of the National Bank Act indicates Congress has defined shareholder rights, duties and liabilities, and the duties and personal liability of directors and officers for violations of the Act. For example, sections 21-40 of the National Bank Act deal with capital, stock, and stockholders, sections 71-78, and 93 deal with directors and their personal liability, section 161 deals with reporting requirements.

## III. The Decisions of the Courts of Appeal as to the Standing of Minority Shareholders to Sue for National Bank Act Violations Are in Conflict.

12 U.S.C. § 93(a), in its present form, was construed by this Court in *Chesbrough v. Woodworth*, 244 U.S. 72, 37 S.Ct. 579 (1917), and this Court there permitted a direct action based upon facts similar to those herein. In *Chesbrough*, a national bank shareholder who purchased stock in reliance upon false reports of the bank's financial condition, and who complained of the payment of dividends out of capital, rather than net profits, was allowed a direct action against the directors. This shareholder was allowed to recover the difference between what he had paid for his stock, less its book value, after deduction of his pro rata share of loss. This Court held that damages in such a case are personal to the shareholder, and do not belong to the association. *Id.* at 482.

The Ninth Circuit, in *Harmsen v. Smith*, 542 F.2d 496 (9th Cir. 1976), held that minority shareholders had standing to sue for violations of the National Bank Act, although their only injuries were damages in the form of diminished stock values. The Court relied upon the language found in 12 U.S.C. § 93(a), which in fact provides a literal grant of standing to shareholders. Despite this literal language, and its prior precedent in *Davis v. McFarland*, 15 F.2d 612 (5th Cir. 1926), *cert. denied*, 273 U.S. 754 (1927), and *Spalitta v. National American Bank of New Orleans*, 444 F.2d 291 (5th Cir. 1971) *cert. denied*, 404 U.S. 883 (1971) (both of these cases are cited by the Ninth Circuit in *Harmsen, supra)*, the Fifth Circuit reversed its prior position and aligned itself in this case with the Sixth Circuit's position as set forth in *Gaff v. FDIC*, 814 F.2d

311 (6th Cir. 1987). The Sixth Circuit in *Gaff* held that stockholders who alleged a diminution in the value of their stock failed to allege a sufficient direct harm to have standing under § 93(a).

This so-called "modern" view is really nothing more than a prudential limitation on standing. As noted, *supra*, courts are not absolutely bound by such court-imposed restrictions on standing. "If Congress has done so, the courts lack authority to create prudential barriers to suits brought under a statute in which Congress has done this." C. Wright, *Law of Federal Courts*, § 13 at 74 (4th ed. 1984), citing *Havens Realty Corp. v. Coleman*, 102 S. Ct. 1114 (1982); *Gladstone Realtors v. Village of Bellwood*, 441 U.S. 91 (1979); *Trafficante v. Metropolitan Life Ins. Co.*, 409 U.S. 205 (1972), ("Many other Acts of Congress appear on their face to contain very broad grants of standing.")

## CONCLUSION

Jurisdiction under RICO, where the rights of minority shareholders of national banks are concerned, should be controlled and governed by a uniform federal law of standing. Standing to sue under RICO in this instance should be the same in all fifty states. Any person injured in his property by reason of a violation of 18 U.S.C. § 1961 *et seq.* should have standing to sue without reference to the law of the state where the loss was sustained, particularly where there are no rights granted under state law to shareholders of national banks. No so-called prudential limitation on standing should exist where the National Bank Act expressly grants standing to persons in the position of Leach.

Respectfully submitted,

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